

China's Development Strategy: The Reality

"What is the chief end of man? To get rich."

-- Mark Twain, 1871

"To get rich is glorious."

-- Deng Xiaoping, 1982

China Pre-Reform



- Danweis and Communes:
 - No labor mobility
 - All benefits paid by the danwei
 - Danwei manage housing, medical care, schooling, death benefits...

Industrial Organization



A “company” consisted of one manufacturing location or one administrative unit, like a school or a trading company. A manufacturer could sell its own products but could not sell anyone else’s.

Challenges

- Social benefits were paid by companies out of pocket
- Right to engage in foreign trade was restricted to government monopolies. Changing this would require enabling access to foreign currency.
- Companies had to sell across geographic lines through local agents. Even if they established their own subsidiaries, transfer of goods, management of bank accounts, payment of taxes were all done on an arm's-length basis.
- System of social and political control was tied entirely to work organizations

How the Economy Was Restructured

- The Creation of Venture Capital
- Privatizing Military Production
- Limited Break-Up of State Monopolies
- Limited Privatization of the National R&D Complex
- The Group Corporation and Companies Limited by Shares
- The Role of Stock Markets

Solutions: Step 1

Venture Capital

- Venturetech, the Chens, and the Dengs: The Beginning of Speculative Investment
- Rong Yiren, the “Red Capitalist,” and Citic

Step 2:

Separating Industry from the Military

- The need for a professional military
- 1988 demobilization and the creation of ZTE and Huawei
- The need for military access to more competitive technologies
- The oligarchs: Wang Zhen's sons and Poly, Great Wall, South Seas Helicopter. Datang, North Industries, Xingxing, etc.

Step 3:

Profiting from Intellectual Property

- Hou Ziqiang and Liu Chuanzhi: Lenovo, Hope Computers, Kejian Handsets
- Jiang Mianheng at CAS: Grace Semi, Netcom
- Jiang's takeover of SAIL, establishment of New Margin, equity stakes in Pudong Airport, China Southern, and much more.
- Universities establish companies: 1994
 - Beida Jade Bird
 - Tsinghua Tongfang

Privatization of R&D

- 2005-6: Intangible equity contributions to companies could exceed 20% of the capital base
- 2003-2005: Two-thirds of the government-supported R&D institutions were required to find their own funding
- This is when China's "tech nationalism" became an international trade issue

Inducements to Establish Companies

- Subsidy Programs
 - Seed Program for Returned Scholars
 - Fund for Returnees
 - Spring Bud, etc.
- Incentive Programs
 - “Green channel” interest-free loans for new business establishment using new technologies
 - Nationally funded incubator program
 - Individual income tax rebates, reduced corporate income tax
- Industrial clustering
 - ~700 tech parks, with subsidized rents and various types of support programs
 - Free IC design tools and other tools of the trade
- Government Outreach
 - MOE and MIIT-funded delegations to recruit IT workers back to China

Step 4:

Limited Break-Up of the Monopolies

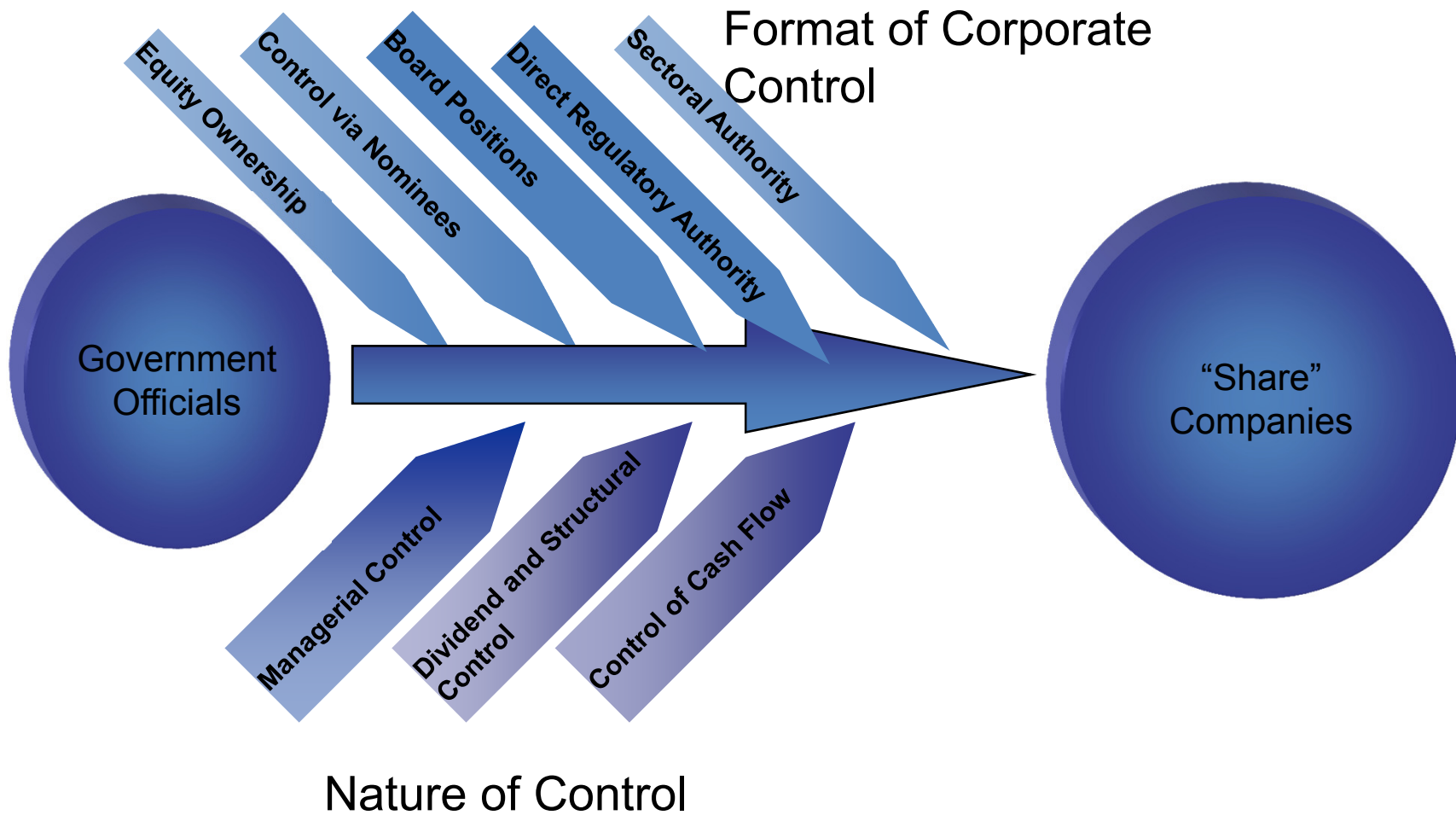
- The goals
 - Introduce competition
 - Maintain state control of distribution networks
 - Reduce government costs by introducing efficiency
- Telecoms: Creation of China Unicom
- “Grasp the Large, Release the Small”: the great 1998 overhaul
 - Restructuring of industrial ministries into trade associations that managed technical standards, statistical functions, subsidies and trade promotion strategies, etc.

Step 5:

New Capital Structures

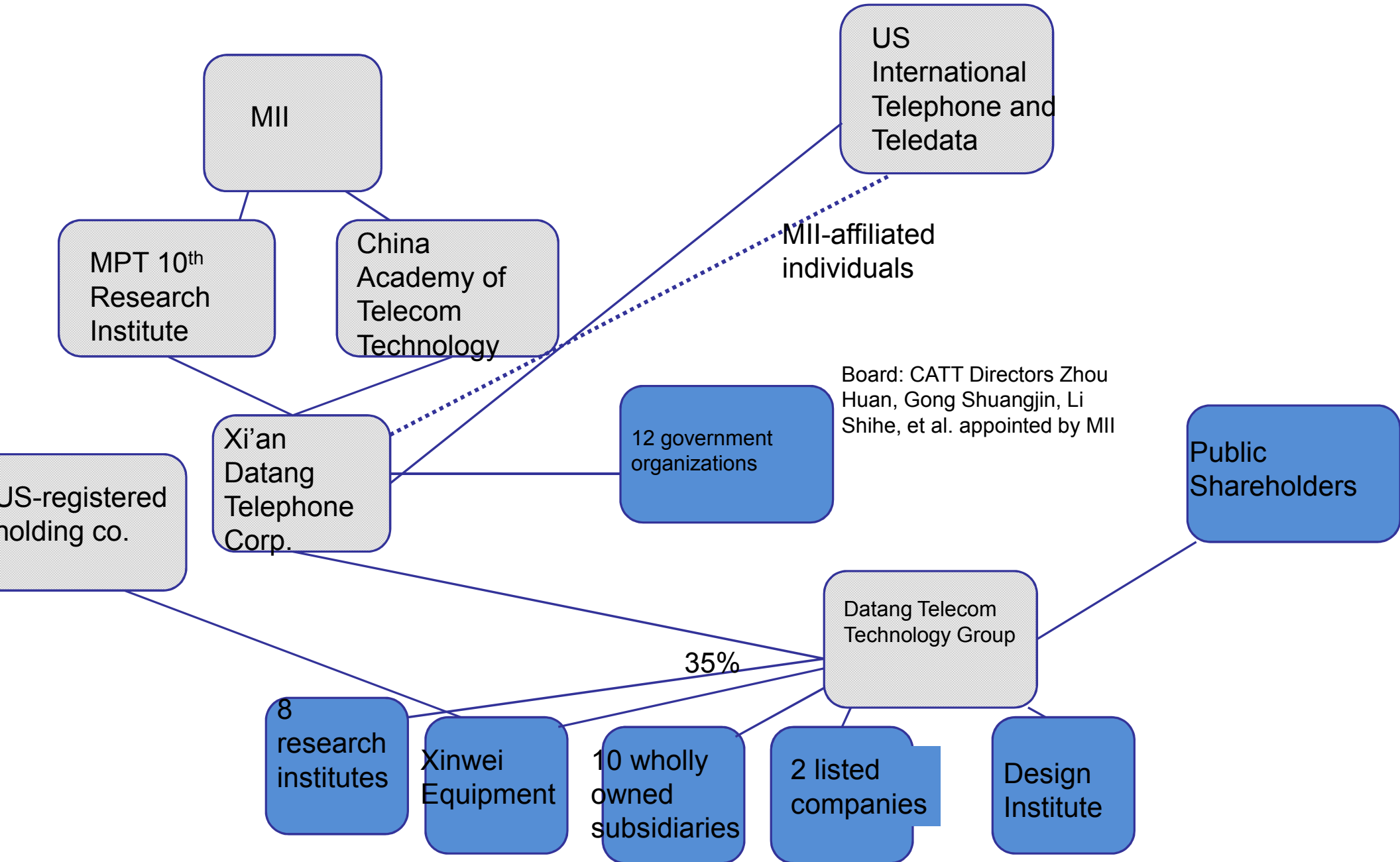
- 1981: Citic proposes issuing a bond in Japan to fund Yizheng Chemical Fibers, leads to a series of “special bonds”
- The Company Limited by Shares: legal basis established 1993, but the format became practical only about five years later
- 1992: Zhu Rongji agrees to let Chinese companies list overseas
- 1997: The “Umbrella Corporation”
- 1997: IPO of China Mobile
- 2000-2002: The Group Corporation

The nature of ownership is changing; it is no longer very clear what is “state” and what is “private.”



Example: Datang

Example: Datang (simplified diagram)



Case Study: Print Media

Pre-1980

- One daily newspaper per city, circulation-supported by subsidized, all delivered by the Post Office
- Magazines published by government agencies or associations in support of their propaganda role
- All editorial content generated by the Propaganda Bureau of the CCP

China's publishing development

- 1980-1990: Growth phase
 - Government subsidies to the media were reduced
 - The number of newspapers grew from about 180 to 2,000
 - Magazines rose from about 400 to about 4,000
 - The commercial advertising market emerged
 - Content became less political and more popular

1990-2000: Market segmentation

- “Second channel” distribution fuels independent publishing
 - Exploiting the bureaucratic battle between the Post Office (national level) and the Beijing Party Committee (local) to achieve a regulatory opening
 - In the early 1990s, publications distribution was still a Postal Administration monopoly. By 2001, there were about 800 independent newspaper-distribution companies
- Enter the Oligarchs
 - In print, people connected with the security bureaucracies were able to obtain publication licenses and to compete
 - Ex: the 999 Group, a break-off from the military, put millions into establishing an independent distribution network
- Readers demand more
 - Page count in newspapers has been increasing in double digits every year
- Quality rises
 - The top publishers are getting stronger and pushing smaller organizations out of business.

2004 on: Consolidation

- Rapid growth of the top 10 publishers
- Emergence of successful group corporations in periodicals
- More financing from private and foreign capital for advertising and distribution

Print Media Today

- Private ownership/financing of advertising and circulation arms
- Rigid supervision of editorial content
- Formal ownership by the government
- Licensing deals bring profit to foreign content owners such as Hearst (Cosmo), National Geographic, Time-Warner (Fortune), etc.
- However, growth is limited. Themes are copied and markets cannibalized. Neither Chinese nor foreign brand owners develop much brand value.